

The auditor performed an extensive review in accordance with these guidelines, and issued its report in July 1992 finding that "the SCIS model is fundamentally sound and provides reasonable estimates of switching system investment attributable to service and feature usage of the switch." Specifically, the auditor found as follows:

- The costing principles inherent in SCIS are appropriate for estimating long run incremental investments attributable to switching system usage, and the specific methods for implementing these principles are reasonable.

- SCIS accurately estimates the cost of actual switching systems engineered according to manufacturer engineering rules as evidenced by Bellcore's validation procedures and results.

- Extensive software development controls and testing are used to assure SCIS models are properly implemented and installed by model users.

- Finally, although SCIS is a complex model requiring considerable understanding of switching systems and service costing, the model documentation, training and technical support are adequate to provide reasonable support for the model in use.<sup>36</sup>

Several of the commenters contend that so much was redacted from the SCIS information that they were unable to make a meaningful analysis of it. Although the intervenors only received a redacted version on the SCIS information, they nevertheless had sufficient information to make a reasonable evaluation based upon what they did have

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<sup>36</sup> "Independent Review of SCIS/SCM", Report, July 1992, Arthur Andersen & Co. SC, p. 7.

available. The intervenors<sup>37</sup> had access to all of the inputs which were used to generate the model office outputs, except the discount. Indeed, intervenors had available to them by far more cost support than has ever been provided in an access tariff proceeding.

As to the actual logic and algorithms of the system, while it is true that the intervenors did not have access to this aspect of SCIS, this is the very reason for which the Commission directed the participation of an independent auditor. The intervenors had the opportunity to meet with the auditor prior to the auditor's review and to submit suggestions to the auditor for matters to be included in the review.<sup>38</sup>

More importantly, cost support information is not for the benefit of intervenors, but rather for the benefit of the Bureau to aid the Bureau in its review. While the participation of intervenors in the tariff review process is an important means of assisting the Bureau in making its own

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<sup>37</sup> Although Allnet received access to the first redacted version of SCIS ("Redaction I"), Allnet did not receive access to the second redacted version ("Redaction II") because Allnet did not comply with the established prerequisites.

<sup>38</sup> In fact, seven of the intervenors attended a meeting with the auditor for this purposes on May 13, 1992, and several submitted written suggestions thereafter. See Ex Parte Notice: Da 92-129, to the Secretary of the Commission from James F. Britt, May 19, 1992, and letters to Arthur Anderson & Co. from AT&T (dated May 21, 1992) and from Ad Hoc and MCI (dated May 22, 1992) all of which were also filed with the Commission.

review, it is not essential that intervenors have access to all of the information upon which the Commission will ultimately make its determination. This is particularly true where the Bureau establishes, as it did here, a process whereby an independent auditor makes an extensive review of the information and data at issue as an aide to the Commission's own review. Given that competitively sensitive information was involved, the Bureau had to strike a balance between the interests of intervenors in participating more fully in the process and the interests of the vendors and Bellcore in protecting their competitively sensitive information.

The main criticism lodged by commenters against the SCIS process is that it is overly sensitive to the various inputs over which each BOC has control. Basically, the contention is that even if the SCIS system itself is sound and reasonable, the direct costs resulting from the process may not be reasonable because the results can only be as sound as the inputs, the auditor did not review the inputs, the BOCs had considerable discretion as to the inputs, and, some commenters speculate, the BOCs could have manipulated inputs and thus BSE costs in an anticompetitive manner.

As a preliminary matter, it was not within the ambit of the auditor's task to review the reasonableness of the inputs, and therefore the auditor necessarily took the inputs at face value and merely showed the extent to which

the SCIS was sensitive<sup>39</sup> to variations in those inputs.<sup>39</sup> Secondly, the Commission has information regarding the inputs, and is capable of reviewing them for their reasonableness. Thirdly, the intervenors themselves had access to the BOC inputs and none of them has shown that the inputs used by BellSouth were manipulated or unreasonable.

Most importantly, BellSouth did not manipulate the inputs used in connection with the SCIS process or in connection with the development of direct costs from SCIS outputs. The manner in which BellSouth determined the direct costs, including the way in which inputs to SCIS were developed, was consistent with the manner in which BellSouth determines the direct costs for identification of the price floor for any other services, whether ONA-related or not, which utilize switching investment. The suggestion that BOC inputs should be even further investigated in this proceeding is to recommend embarkation upon yet another fishing expedition. By far, more cost support has been provided in this proceeding than ever before since the Commission's access charge rules took effect, and the impact of such level of scrutiny of costs is to turn Price Cap

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<sup>39</sup> Similarly, the auditor did not evaluate the BOCs' ratemaking processes as these were also not within the scope of the referral. Indeed, auditor review of ratemaking processes was not necessary, as the Bureau and the intervenors have substantial information from which they can make their independent reviews to evaluate whether such processes were within the guidelines of the Commission's "flexible cost-based approach" to pricing.

regulation on its head such that, contrary to the Commission's stated intentions for Price Cap regulation, BOCs are subject to even greater cost burdens than they experienced under rate of return regulation. The Bureau should apply the intended spirit of Price Cap regulation -- i.e., departure from rate of return-based principles of regulation and encouragement of pricing flexibility -- in its determinations of the matters under investigation here.

Nevertheless, BellSouth here responds to the allegations of those intervenors which have raised specific questions about specific BOC decisions and inputs, and shows that BellSouth's were reasonable. Of those specific matters highlighted by the intervenors, BellSouth has already justified the use of many, for instance, the use of a long-run incremental cost approach, the use of the marginal option of SCIS, the use of digital technology, and the use of a forward-looking cost of money factor in developing annual charge factors.

Several parties suggest that BOCs may have used outdated versions of SCIS, although only AT&T singles out BellSouth in particular. Although additional versions of SCIS have been made available since BellSouth conducted its studies, BellSouth used the most recent versions of SCIS available at the time it performed such studies.

Furthermore, as the Bureau<sup>40</sup> will see from Appendix 21 of the auditor's report, the change in SCIS versions from those utilized by BellSouth and the more recent versions is minuscule.

Ad Hoc, through its consultant, contends that the Bureau should require BOCs to use EF&I investment inputs in lieu of material prices. Although BellSouth did use only EF&I investment inputs, Ad Hoc is incorrect that the Bureau should impose this as a requirement. If a BOC has more accurate accounts of the actual engineering and furnishing components, then it would be correct to use those actual data. For all of the reasons stated above, in Section II. supra, it is simply inappropriate and unnecessary for the Bureau to impose this type of uniformity upon the BOCs.

AT&T states that BellSouth used "outdated" inputs into SCIS model office development. While it is true that BellSouth development of the model offices were based upon 1989 Busy Season data, such data reflects BellSouth's determination of the usage characteristics for the central office. A central office is not designed for only one, two or three years, but rather for the long-term, and to do otherwise would be uneconomical. Thus, the model office input data should not fluctuate to any great extent year over year.

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<sup>40</sup> Appendix 21 was redacted from Redaction II and therefore not available to intervenors.

In summary, the Bureau has more than sufficient information before it to determine whether or not the BOCs' costing methodologies are reasonable and within the parameters of the Commission's "flexible, cost-based approach" for pricing new services. As the auditor has reported, the SCIS processes used to identify investment are reasonable. Furthermore, BellSouth utilized a means to develop inputs to the SCIS processes consistent with the develop of inputs for other services for which SCIS is utilized to identify the price floor of new services. No further adjustment of or inquiry into BellSouth's cost methodologies is needed.

#### V. MISCELLANEOUS ISSUES

Sprint raises a miscellaneous issue regarding conversion. It requests clarification from the BOCs regarding the extent to which conversion of a customer's existing circuits from a bundled feature group offering to an unbundled offering will result in traffic routing changes.<sup>41</sup> For BellSouth, the conversion of existing feature groups to their unbunbled equivalents requires changes only in the associated records, and does not require any physical change in routing.

#### VI. CONCLUSION

In this proceeding, BellSouth has fully responded to the issues designated for investigation, as well as the

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<sup>41</sup> Sprint, p. 9, n. 11.

additional SCIS-related issues specified by the Commission. BellSouth appropriately developed costs, using the SCIS processes, of its BSEs to identify the price floor for each of its BSEs, and applied reasonable loadings to such costs to arrive at the final BSE rates. Sufficient time and effort has been expended in this proceeding, and the Bureau should conclude its investigation forthwith and allow all concerned to move forward to tackle the more pressing issues at bay.<sup>42</sup>

Above all, the Bureau should keep in mind that its review of BOCs' BSE rates must be consistent with both the letter and the spirit of the pricing standards established by the Commission, i.e., the use of a "flexible, cost-based approach" to the pricing of new services. This standard does not mandate uniformity in costing and pricing methodologies either from BOC to BOC or from service to service within a BOC's own operations. Rather, the Commission's pricing standard provides BOC's with a measure

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<sup>42</sup> Expanded Interconnection with Local Telephone Company Facilities, Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 91-141 - Transport Phases I & II, CC Docket No. 80-286, Second Notice of Proposed Rulemaking (FCC 92-441), released October 16, 1992; Transport Rate Structure and Pricing, Petition for Waiver of the Transport Rules filed by GTE, CC Docket No. 91-213, Report and Order and Further Notice of Proposed Rulemaking (FCC 92-442), released October 16, 1992; Expanded Interconnection with Local Telephone Company Facilities, Amendment of the Part 69 Allocation of General Support Facility Costs, CC Docket Nos. 91-141 and 92-222, Report and Order and Notice of Proposed Rulemaking (FCC 92-440), released October 19, 1992; Intelligent Networks, CC Docket No. 91-346, Notice of Inquiry, 6 FCC Rcd 7256 (1991).



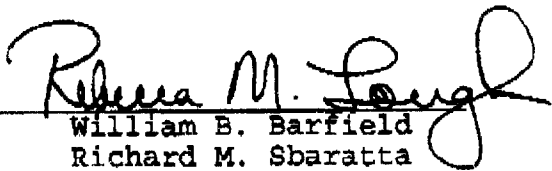
of pricing flexibility which - although, in BellSouth's opinion, is not nearly the extent of flexibility appropriate in the increasingly competitive access environment of today - is clearly broad enough to support the costing and pricing methodologies utilized by BellSouth to develop the rates under investigation here.

Finally, the Bureau should reject any and all suggestions that it should micromanage the BOCs' new service filings, be they ONA or otherwise. To follow this path would be a regression back to rate of return, fully distributed cost regulation, a path wholly incompatible with the progression toward a competitive, market based approach which BOCs must be afforded in order for there to exist an even playing field vis-a-vis their competitors.

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DATE: November 13, 1992

CERTIFICATE OF SERVICE

I hereby certify that I have this 13th day of November, 1992 serviced all parties to this action with a copy of the foregoing REBUTTAL by placing a true and correct copy of same in the United States mail, postage prepaid, to those persons listed on the attached service list.

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